EXECUTIVE SUMMARY

The services sector now accounts for over 70% of total employment and value added in OECD economies. It also accounts for almost all employment growth in the OECD area. But despite its growing weight, productivity growth in services has been slow in many OECD countries and the share of the working-age population employed in services remains low in many countries. If policy makers wish to strengthen economic growth and improve the foundations for the future performance of OECD economies, the services sector will need to do better. But strengthening growth performance is not the only challenge facing policy makers; OECD countries are also confronted with the growing globalisation of services and manufacturing and with rapid technological change. This has raised doubts about the capacity of OECD economies to create new jobs, while at the same time offering new opportunities for international trade and investment. Addressing these challenges and strengthening the potential of services to foster employment, productivity and innovation will need to build on sound macroeconomic fundamentals and involve a combination of structural policies. This OECD services compendium encourages policy makers to take action in the following areas:

Open domestic services markets to create new job opportunities and foster innovation and productivity. Further regulatory reform of services markets will create fresh opportunities for firms to develop new services, meet emerging global demands and increase employment. It will also increase the incentives for companies to innovate and improve productivity growth. While much progress has been made in opening services markets, further steps are needed, *e.g.* in reducing the degree of public ownership in competitive industries such as air transport, in addressing anti-competitive practices in professional services, and in reducing barriers to entrepreneurship.

Take unilateral and multilateral steps to open international markets to trade and investment in services. OECD work shows that the benefits of international trade and investment in services are highly significant, for both OECD economies and developing countries. Policy makers can take unilateral steps to open markets to international competition, for instance by reducing barriers to foreign direct investment. At the same time, multilateral action is needed to ensure a broad opening of markets and a wide distribution of the benefits. OECD members should therefore seize the opportunities offered by the ongoing WTO Doha negotiations to open their services markets.

Reform labour markets to enable employment creation and adjustment to a growing services economy. Effective labour and social policies are essential to help OECD economies adjust to globalisation, structural change and the shift to services. To strengthen employment creation in services, policy makers should address high labour taxes that affect the job prospects for low-skilled workers and the development of personal services in OECD economies. Employment protection legislation should be reformed in countries where it is overly strict, to help improve the capacity of these economies to create employment and enhance productivity growth in services.

Adapt education and training policies to rapidly changing requirements for new skills. Since most services involve direct contact with customers, human resources are key to services sector performance. Education policies are important to help workers adjust to globalisation and structural change and should help provide the qualifications that are needed in services. However, they need to

be supplemented with actions, partnerships and co-financing by firms, workers and governments to foster life-long learning. This will require improved incentives for private financing of life-long learning and actions to ensure equitable access to formal and on-the-job learning.

Adapt innovation policies to the growing importance of services innovation. Innovation policies remain ill adapted to the growing importance of innovation in services, and to the new potential for product and process innovation that is due to information and communication technology (ICT). Policy makers should consider how existing public research and development (R&D) can better address the needs of the services sector and improve the links between services sector firms and public research. In modifying policies related to intellectual property in services, governments will need to strike a careful balance between innovation and the diffusion of service innovations to other industries.

Remove impediments that prevent services firms from seizing the benefits of ICT. To seize the benefits of ICT for services, governments should continue to encourage effective competition in ICT infrastructure, network services and applications, notably for broadband. They will also need to increase the trust in electronic business, *e.g.* by developing effective regulatory frameworks. Regulatory barriers, *e.g.* to digital delivery and digital content, also require reform, as they are not adapted to the new potential offered by electronic business. Moreover, governments can take action themselves, by developing public services and digital content.

Provide a fiscal environment which is conducive to the growth of services. Governments will need to avoid that the interaction between the application of European Union (EU) and non-EU value added taxes, as well as sales taxes, leads to new tax barriers to cross-border services. Tax treaties should be reviewed to avoid such activities being subject to double taxation. Tax dispute settlement procedures should be accelerated and reinforced, notably for cross-border services and intangibles.

Reform of services sector policies provides an important opportunity for policy makers to strengthen employment, productivity and innovation. It will also help in strengthening the capacity of OECD economies to adjust to economic globalisation in services and to the growing importance of services to future growth in OECD economies. The policies advocated in this report are mutually reinforcing. This is important since seizing the new growth opportunities in the services sector and adjusting to globalisation will be possible only through a comprehensive strategy based on a policy mix that is suited to each country or circumstance.

With so many policy areas affecting the services sector, priorities are essential, however. Moving quickly towards more open and competitive services markets, at both the national and international level, is of the greatest importance to foster new employment opportunities and increase innovation and technology diffusion. This also means providing more scope for entrepreneurs to explore the new business opportunities in the services sector, in particular at the global level, and providing a fiscal environment that is conducive to the growth of services. At the same time, improvements in the functioning of labour markets and institutions are urgently needed to help OECD economies adjust to globalisation and the shift to services. Education and training policies clearly have a key role in providing workers with the new skills they will require in an increasingly global service economy. Also, much can be done to improve policies related to innovation and ICT in services, as the combination of ICT and process innovation holds the key to generating more rapid innovation and productivity growth in the services sector. In all these areas, it will also be important to account for the large diversity of the services sector and the resulting variety in policy challenges and growth prospects.

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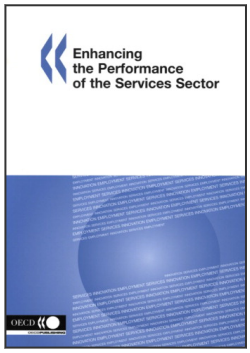

From:

Enhancing the Performance of the Services Sector

Access the complete publication at:
https://doi.org/10.1787/9789264010307-en

Please cite this chapter as:

OECD (2006), "Executive Summary", in *Enhancing the Performance of the Services Sector*, OECD Publishing, Paris.

DOI: https://doi.org/10.1787/9789264010307-2-en

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